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FM AMEMBASSY HARARE
TO RUEHC/SECSTATE WASHDC IMMEDIATE 4694
INFO RUCNSAD/SOUTHERN AF DEVELOPMENT COMMUNITY COLLECTIVE
RUEHAR/AMEMBASSY ACCRA 2935
RUEHDS/AMEMBASSY ADDIS ABABA 3053
RUEHRL/AMEMBASSY BERLIN 1482
RUEHBY/AMEMBASSY CANBERRA 2316
RUEHDK/AMEMBASSY DAKAR 2683
RUEHKM/AMEMBASSY KAMPALA 3101
RUEHNR/AMEMBASSY NAIROBI 5544
RUEAIIA/CIA WASHDC
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RHMFISS/EUCOM POLAD VAIHINGEN GE
RHEFDIA/DIA WASHDC
RUEHGV/USMISSION GENEVA 2231
RHEHAAA/NSC WASHDC

UNCLAS SECTION 01 OF 04 HARARE 000559

SENSITIVE
SIPDIS

AF/S FOR B. WALCH
DRL FOR N. WILETT
ADDIS ABABA FOR USAU
ADDIS ABABA FOR ACSS
STATE PASS TO USAID FOR J. HARMON AND L. DOBBINS
STATE PASS TO NSC FOR SENIOR AFRICA DIRECTOR MICHELLE GAVIN

E.O. 12958: N/A
TAGS: EINV ECON EMIN ETRD PGOV PHUM PREL ZI
SUBJECT: ZIMBABWEAN FIRMS EXPRESS GUARDED OPTIMISM ON
RECOVERY

REF: HARARE 531

SUMMARY

¶1. (SBU) Discussions with a cross-section of Zimbabwean businesses indicated the sector is eager to contribute positively to economic recovery and feels more optimistic about the country's economic future than it did prior regulatory liberalization (including dollarization) that has led to price stability. However, further recovery has stalled due to a number of constraints that include excessively high wage demands by labor (reftel), limited access t credit and unfavorable terms, high utility costs, and an adverse political environment that deters outside investment. It is critical that these issues, particularly access to meaningful credit, be resolved urgently or Zimbabwe risks further manufacturing sector decline in the face of South African competition. More political reforms guaranteeing the rule of law and the restoration of property rights are crucial for increased investment that will buttress economic recovery. (END SUMMARY).

Relief Giving Way to Confidence

¶2. (SBU) Econoff and econ specialist met in mid-June with a range of Zimbabwean business leaders, representing the agricultural, apparel, finance, and manufacturing sectors, to assess their outlook on Zimbabwe's economic fortunes. These executives praised the stabilization of the economy since dollarization and the adoption of market-friendly reforms. Industry umbrella group the Confederation of Zimbabwe Industries (CZI) welcomed the Short Term Economic Recovery Program (STERP) because it reflected a major paradigm shift toward a holistic approach including political reforms that previous recovery programs had ignored. The resultant price

stability has stemmed the outflow of skilled labor, made business planning viable again, and eased fears of arrest and prosecution for circumventing unproductive policies.

¶3. (SBU) Dumisani Sibanda, President of the Matabeleland Chamber of Industries, told us workers are confident they will be paid on a regular basis and their salaries will hold value, resulting in less absenteeism. Chitranjan Laxmidas, Managing Director of apparel manufacturing firm Style International, said his company had budgeted on a daily basis over the past five years, and during the peak of hyper-inflation last year it was making pricing decisions on a two-hour basis. Sibanda and Tony Rowland, CEO of agricultural equipment manufacturer Zimplow, noted they no longer worry about being jailed for running afoul of price controls or other state policies that had stifled business until changes were adopted in February and March.

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Sector Repositioning to Capitalize on Stable Conditions
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¶4. (SBU) Some companies are taking advantage of the improved
Q4. (SBU) Some companies are taking advantage of the improved
environment to reposition their businesses or enter new markets. Lishon Chipango, the Chairman of Interfresh Limited, a producer of cut flowers, mixed vegetables, maize, soy beans and citrus, told econoff on June 16 that Interfresh is currently shifting towards better margin mixed vegetables and retail activities, which helps to off-set reduced demand for their flower exports and grains.

¶5. (SBU) Apparel manufacturers are spreading their risks by repositioning themselves to go global in the face of falling domestic demand. For example, Laxmidas told us his company is expanding from mainly supplying the U.S. market to entering the South African, East African, Asian, and European markets. Similarly, David Lasker, Chief Executive Officer of Archer Clothing Manufacturers Private Limited, is refocusing exports from a few select European markets to the SADC and other regions. He also said that his company is about to re-enter the Italian and German markets, and is positioned to access the Australian market for the first time. Rowland mentioned that, unlike most Zimbabwean companies, Zimplow is doing well enough to raise working capital without having to borrow because of its long history of exporting. He explained that Zimplow has to offer better quality and after-sale services to compete with Chinese and Indian products that under-cut by half his prices in East African markets.

Yet Major Challenges Remain

¶6. (SBU) Despite the overall positive mood, every businessperson with whom we spoke emphasized the need to resolve a number of constraints such as high wage demands by labor (reftel), limited credit access and unfavorable terms, high utility costs, and the adverse political environment. Manufacturers told us that these constraints are stifling both utilization of existing capacity and new investment. Sibanda told us that businesses in Matabeleland are operating at about 15 percent capacity on average. Two of Zimplow's operations are running at only 10 percent capacity while the third is at 35 percent. The latter operation benefited from the farm mechanization program that created government-driven demand for Zimplow's animal-drawn equipment. Although payment for the implements was made in Zimbabwe dollars by the Reserve Bank of Zimbabwe, the company immediately exchanged the local currency on the parallel market for foreign exchange. Style International is operating at 20-25 percent capacity. Diamond and platinum miners reported the highest capacity at over 90 percent.

Lack of Credit and Terms Stifling Investment

¶7. (SBU) All companies visited expressed a desire to recapitalize their operations after a decade of infrastructural erosion due to lack of investment. Laxmidas told us that most companies were now only worth around 5 percent of their previous value due to years of hyperinflation. Most companies complained that few long-term credit facilities exist and that the terms, such as interest rates, are un-affordably high. Zimbabwean banks do not have money to lend because of a lack of deposits. External lines of credit are small, short-lived, and expensive. Businesses
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complained of prohibitive roll-over costs when attempting to extend existing credit facilities.

¶8. (SBU) Chipango cited loans being offered by foreign banks Afrexim and PTA with rates of between 9 and 13.5 percent attached to strict vetting criteria. M.D. Moyo, the General Manager of cement maker Sino-Zimbabwe, applied for a US$2 million loan from a local bank but was offered only a US$200,000 loan on stringent terms, including repayment within six months and submission of the curriculum vitae of all the company's top management. Laxmidas was offered 8

percent money for three months plus 2.5 to 3 percent rollover fees every three months. Lasker said these sorts of expensive, short-term loans effectively amount to annual rates exceeding 20 percent, making borrowing untenable in a global environment where foreign companies can access credit at 1.5 to 2 percent. This discrepancy is causing some companies such as Zimplow to lobby for temporary tariff protection against imports.

Utilities Grossly Overpriced

¶9. (SBU) Every businessperson we interviewed pointed to high utility costs as a major obstacle to improving efficiency. They blamed a hyperinflationary mindset and a lack of understanding that dollarization meant stable prices. National Railways of Zimbabwe (NRZ) is considered a prime offender. Moyo said that it is cheaper to transport his company's product by road than by rail. Lasker noted that his company uses only private transport companies because of poor reliability of Zimbabwe's railways. According to Moyo, allowing some utility companies pricing flexibility would benefit the cement industry. He gave the example of the Zimbabwe Iron and Steel Company (ZISCO) whose only current source of income is from selling slag -- a steel byproduct that other producers in the region give away -- because price controls have made steel production unprofitable. The additional charge of paying for slag adds to Sino-Zimbabwe's input costs and reduces the competitiveness of its cement on both the local and foreign markets.

¶10. (SBU) Similarly, Laxmidas and Rowland complained about exorbitant phone bills. Both showed econ specialist recent charges. For example, one branch of Style International was charged more than US$600 for a month of service. A residential phone belonging to the company was billed over US$300. Rowland and Group Financial Director of Treger Holdings, Charmaine Kerr, stressed the need for prices of utilities to be at par with regional prices, yet they are currently five to ten times higher than in South Africa.

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Political Environment/Policies Harming Progress
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¶11. (SBU) Companies blamed an adverse political environment

for deterring investment and noted the need for more policy changes in order to boost operations. Moyo at Sino-Zimbabwe noted that even though exporting companies can claim back value added tax at a later date, they should be exempted from paying the tax because it ties up working capital. He was also unhappy with the long time taken to process export permits by the Ministry of Industry and Commerce even after ZIMRA, the local customs authority, completes their normal checks. Moyo stated that this delays the shipment of goods and hurts exports. Moyo does not expect further improvements
Qand hurts exports. Moyo does not expect further improvements
until the political environment changes. Sibanda believed that tax collection should revert back to the bi-annual system that existed prior to hyperinflationary times. For now, taxes are still being collected every quarter, which prevents businesses from having cash on hand to fund working capital.

COMMENT

¶12. (SBU) Overall, the mood within the business community is

optimistic following dollarization and the institution of market-friendly reforms. However, major challenges remain. Zimbabwean businesses that survived hyperinflation are now struggling to adjust to high labor costs, excessive utility charges, poor service delivery, and lack of affordable credit due to a domestic banking liquidity crisis. Additionally, a political risk premium attached to conducting business in Zimbabwe remains because of inconsistent government policies and security of investment concerns. END COMMENT.

DHANANI